EFFICIENT GROUP

ECONOMIC COMMENTARY

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YOUR WEEKLY ECONOMIC UPDATE

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DO NOT PANIC, MANAGE YOUR RISK, AND BUY THE DIP

During the first week of May, the Federal Reserve (Fed) in the United States (US) increased interest rates by 0.5%, the first time since 2000. Later, during the last week of the month, the South African Reserve Bank (SARB) followed suit. We agreed with the decision of the Fed but disagreed strongly with the decision of the SARB. While inflation in the US is exceptionally high, in fact, at a 40-year high, inflation in South Africa (SA) is not expected to breach the SARB's upper limit of 6% this year. Whereas consumers in the US have just come out of the 10 greatest years of wealth accumulation, consumers in SA have faced one hardship after the other. Unemployment in the US was recently still at record lows, whereas unemployment in SA is still setting record highs. While South Africans struggle to secure employment, there are still more job vacancies than unemployed individuals in the US. And so, the list goes on.

Even though the Fed has made it abundantly clear that they are aware of the impact of their decisions on the US economy, showing that they are unwilling to risk forcing the US economy into a recession, investors are still fearful of a policy error. The month of May, therefore, brought no relief to markets or the weary, fearful investors that they represent. After what appeared to be a strong start, even the Johannesburg Stock Exchange (JSE) gave up its gains. Year-to-date, the JSE was down more than 7% at the end of May. Luckily, this is nowhere near the year-to-date contraction of roughly 26% that we have seen on the technology-heavy Nasdaq Composite. But interest rate concerns are not the only drag on markets.

Markets have been worn out by the ongoing war in Ukraine and its impact on livelihoods, inflation, and global growth. There has also been a lot of concern about China's zero-COVID policies that have caused work stoppages at ports and factories, which have fuelled the property slump and fears about a global recession. But we have continually reiterated that China has their reputation to protect, both externally and internally. In true form, the Chinese central bank then announced that they would reduce one of their key interest rates. The five-year prime loan rate that governs how lenders base their mortgage rates was cut from 4.60% to 4.45%. This decrease will not only boost market sentiment and demand but should also ease global recession fears.

In general, I, therefore, still believe that the markets are slightly overreacting. I am not saying that a recession is not possible, but even if this is the case, recessions usually do not last too long; in the US, recessions are typically between 15 and 17 months. All the market volatility that we have been experiencing is, therefore, the perfect buying opportunity. It is not the time to be getting out of the market but, like Warren Buffett, we are greedy when others are fearful.

So, if you are still saving towards a specific goal, like retirement, do not stop, but rather continue adding to your investment. Maybe also consider increasing your allocation. This will reduce your average entry price, which will increase your long-term potential returns. If you are retired, ensure that you have managed your risk appropriately, that is, that you have enough income to get you through this short-term volatility (up to two years) so that you do not have to realise your losses and sell out of your equity positions. In the odd case that you are over-exposed and have not been managing your risk appropriately, speak to your financial advisor. But most of all, do not panic!

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